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CHARLES ELMORE CROPLEY
CLERK

Supreme Court of the United States

OCTOBER TERM, 1941.

No. 781.

ROYAL INDEMNITY COMPANY, - - - Petitioner,

versus

UNITED STATES OF AMERICA, - - - Respondent.

Petition for Writ of Certiorari to the United States Circuit Court of Appeals for the Sixth Circuit and Brief in Support Thereof.

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Louisville, Kentucky.

WESTERFIELD-BONTE CO., INCORPORATED, LOUISVILLE, KY.



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Supreme Court of the United States

OCTOBER TERM, 1941.

No._____

ROYAL INDEMNITY COMPANY, - - *Petitioner,*

v.

UNITED STATES OF AMERICA, - - *Respondent.*

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT.

To the Honorable, the Supreme Court of the United States:

Your petitioner respectfully shows:

I.

SUMMARY STATEMENT OF THE MATTER INVOLVED.

In the year 1918 Louisville Woolen Mills and three other corporations were wholly owned by American Textile Woolen Company. The five corporations were therefore affiliated within the meaning of Section 240 of the Revenue Act of 1918, which mandatorily required that affiliated corporations should make a con-

solidated return instead of individual returns, and that the tax should be computed upon such consolidated return and assessed upon the respective affiliated corporations in such proportions as may have been agreed upon among them, or in the absence of any such agreement, on the basis of the net income properly assignable to each.

Notwithstanding the mandatory provisions of Section 240, the Louisville Woolen Mills and its affiliates did not file a consolidated return for the tax year 1918, but each filed an individual return. In due course there was assessed against each of the affiliates the tax shown to be due on their respective individual returns. Within the time provided by law the Louisville Woolen Mills paid three quarterly installments of the tax assessed against it on its individual return, but shortly before December 15, 1919, the date on which the last installment, amounting to $32,341.24, became due, it filed with the Commissioner of Internal Revenue a request that the balance of the assessment be abated by giving it the benefit of a special assessment as authorized by Sections 327 and 328 of the Revenue Act of 1918 (which in substance authorized the Commissioner, if he found that owing to abnormal conditions affecting the capital or income of a corporation assessment of the tax under the general provisions of the Act would work upon such corporation an exceptional hardship, to assess the tax against such corporation so that the tax would bear the same ratio to the net income of the taxpayer as the average tax of representative corporations engaged in like or similar trade

or business bore to their average net income). At the time the claim for abatement was filed Louisville Woolen Mills asked that payment of the fourth installment be postponed until its claim for abatement had been acted upon by the Commissioner, which request was granted, the taxpayer being required, however, to execute the following bond:

"Know All Men By These Presents:

That the Louisville Woolen Mills, a Kentucky corporation, doing business in Louisville, Kentucky, where their offices are, has this day filed Form 47, asking an abatement of their tax in the sum of $32,341.24.

"Now, Therefore, in consideration of withholding collection and of said taxes at this time and until such time as the Honorable Commissioner of Internal Revenue may pass upon the claim for abatement of said assessed taxes filed by the principal herein, and in order to protect the United States Government and Elwood Hamilton, Collector of Internal Revenue of the Kentucky District, against any loss, cost or damage by reason of the said claim for abatement, the Louisville Woolen Mills, of Louisville, Kentucky, principal, and the Royal Indemnity Company, of New York, surety, hereby bind themselves, jointly and severally, and their several heirs, executors, administrators, successors and assigns to pay to the said Elwood Hamilton, Collector of Internal Revenue in and for the Collection District of Kentucky, the sum of $32,341.24, or as much thereof, if any, as the said Louisville Woolen Mills may be required

by the United States of America to pay on account of said assessment, together with interest thereon at the rate of one per cent per month from the 15th day of December, 1919, and together with all costs and penalties thereon; and the said principal and surety do further bind themselves, jointly and severally, their several heirs, executors, administrators, successors and assigns, to hold the said Elwood Hamilton, Collector of Internal Revenue as aforesaid, entirely harmless from all loss, costs, and damages he may sustain by reason of his having given to the said principal, that is, the Louisville Woolen Mills, an extension of time within which to obtain a final ruling from the Honorable Commissioner of Internal Revenue as to the liability of the said Louisville Woolen Mills for the said assessment; and, further, to pay the sum of $32,341.24, or as much thereof, if any, as the Honorable Commissioner of Internal Revenue shall find from his rulings to be due to the United States of America from the said Louisville Woolen Mills on account of the said assessment, with interest thereon at the rate of one per cent per month from the 15th day of December, 1919, together with all costs and penalties thereon which may accrue.

"In Testimony Whereof, witness the signature of the Louisville Woolen Mills, as principal, and the Royal Indemnity Company, of New York, as surety, this 15th day of December, 1919.

Louisville Woolen Mills,
Per R. H. Wintersmith, Agent.

Royal Indemnity Company,
By Henry C. Bedinger,
Atty. in fact."

At the time this bond was executed no consolidated return had been filed by the Louisville Woolen Mills or any of its affiliates.

Nearly one year after the execution of the bond, and without having theretofore disposed of the claim for abatement, the Commissioner ruled that the Louisville Woolen Mills and the other corporations hereinbefore referred to were affiliated within the meaning of Section 240 of the Revenue Act of 1918, and that a consolidated return instead of individual returns should be filed for that year. In accordance with such ruling the parent company, American Textile Woolen Company, filed such consolidated return. Thereafter the Commissioner ruled that an agreement existed between the corporations to the effect that all of the tax shown to be due on the consolidated return should be assessed against the parent corporation alone, and he accordingly proposed such an assessment.

At this stage of the proceeding, and in reliance upon the Commissioner's ruling that a consolidated return was required and that the tax assessed in respect thereof should all be paid by the parent company, Louisville Woolen Mills contributed to the parent company $30,000 toward the consolidated tax liability, which amount, together with other funds, was turned over by the parent company to the Collector as a payment on account of the ultimate consolidated liability.

The parent company then appealed to the Board of Tax Appeals from the Commissioner's decision and ruling to the effect that an agreement existed between

the parent company and its affiliates under which all the tax resulting from the consolidated return should be assessed against the parent company. While Louisville Woolen Mills and the other three subsidiaries of the parent company were originally permitted to appear in the Board of Tax Appeals case, subsequently at the hearing an order was made eliminating them on the ground that they were not proper parties to the appeal. The Board of Tax Appeals upheld the Commissioner in his contention that there was an agreement between the corporations that all the tax shown to be due by the consolidated return should be assessed against the parent company alone. The opinion of the Board was rendered June 12, 1931, and final order under Rule 50 of that Board was entered on January 16, 1932 (23 B. T. A. 670). The parent company appealed to the Circuit Court of Appeals for the Sixth Circuit, which affirmed the Board (68 Fed. (2d) 820). This Court denied certiorari (293 U. S. 558).

During the entire period of twelve years and one month which intervened between the filing of the claim for abatement and execution of the bond, and the entry of the order of the Board of Tax Appeals, the Commissioner made no ruling that Louisville Woolen Mills was liable for any amount of tax on account of the assessment made on its individual 1918 return. However, on August 23, 1932, which was twelve years and eight months after the execution of the bond, and more than one year and two months after the Board of Tax Appeals had decided that all of the taxes of the affiliated corporations for the year 1918 were assess-

able against and collectible from the parent corporation, American Textile Woolen Company, alone, the Commissioner undertook to fix liability on the bond in the following letter addressed to Louisville Woolen Mills:

> "Your claim is for abatement of part of the tax reported on your separate 1918 return and is a claim for special assessment under Sections 327 and 328 of the Revenue Act of 1918. During the year 1918 your company was a subsidiary of American Textile Woolen Company, and computation of the profits tax of the consolidation under Sections 327 and 328 of the Revenue Act of 1918 was allowed by the Bureau. The Bureau's computation of the consolidated tax was appealed to the United States Board of Tax Appeals by your parent company on an issue relative to the allocation of the tax, and the Board's order entered January 16, 1932, in effect allocates to your company the amount of tax previously assessed on your return. Your claim for the abatement of part of such assessment will therefore be rejected."

At the time said letter was written Louisville Woolen Mills was hopelessly insolvent and paid no part of the sum mentioned in the bond, and thereupon demand was made upon the surety, Royal Indemnity Company, petitioner herein, for payment, and payment was refused upon the ground that there had been no breach of the bond. Suit was then brought in the United States District Court for the Western District of Kentucky to recover on the bond. The case was

tried upon the pleadings, which set out the facts as hereinabove stated. The District Court gave judgment against the surety, petitioner herein, for the full amount of the bond plus interest, but denied it the benefit of the contribution of $30,000 made by the Louisville Woolen Mills to the parent company toward the consolidated liability, and that judgment has been affirmed by the Circuit Court of Appeals for the Sixth Circuit (120 Fed. (2d) 136). A copy of the opinion of the Circuit Court of Appeals is appended to this petition as an appendix.

II.

JURISDICTION OF THIS COURT.

Section 347 of Title 28, U. S. C. A. (Section 240 of the Judicial Code), is relied upon to sustain the jurisdiction of this Court to review the judgment of the Circuit Court of Appeals for the Sixth Circuit herein sought to be reviewed. The opinion in that case was delivered on June 4, 1941. A petition for rehearing was filed in due course, and that petition finally denied by an order entered on the 9th day of October, 1941. This petition is filed within three months from that date, as provided in Section 350, Title 28, U. S. C. A. (Section 240(c) of the Judicial Code).

III.

QUESTIONS PRESENTED.

The opinion of the Circuit Court of Appeals for the Sixth Circuit holds:

(1) That the fact that the Board of Tax Appeals and the Circuit Court of Appeals had judicially and finally determined that the taxes for the year 1918 were assessable against and collectible from the parent corporation alone was not a bar to the Commissioner making a ruling on the bond that the subsidiary owed the tax individually;

(2) That notwithstanding a consolidated return by the affiliated corporations was mandatorily required by Section 240 of the Revenue Act of 1918, and notwithstanding there was an agreement between the corporations that all of the tax shown to be due by such consolidated return should be assessed against and paid by the parent corporation, nevertheless the status of the Louisville Woolen Mills, the principal on the bond, in respect of the consolidated taxes for the year 1918, was that of a taxpayer; and

(3) That the payment of $30,000 by the Louisville Woolen Mills to the parent company as a contribution toward the consolidated liability, made after the giving of the bond and after the Commissioner had ruled that a consolidated return alone was proper and that the entire tax shown to be due thereon was assessable against the parent company, and in reliance upon such ruling, did not

as of the date of payment operate to reduce the liability of the surety to the extent of such payment.

It is believed that these rulings of the Court below are erroneous, and these are the questions presented in this proceeding.

IV.

REASONS RELIED ON FOR ALLOWANCE OF THE WRIT.

(1) The Circuit Court of Appeals, in holding that the surety on a tax abatement bond was bound by the ruling of the Commissioner that the principal was liable for the taxes in respect of which the bond was executed, made after the Board of Tax Appeals and the Appellate Court had finally determined that there was no liability on the part of the principal in respect of such taxes, decided an important question of federal law which has not been, but should be, decided by this Court.

(2) The Circuit Court of Appeals, in deciding that notwithstanding the requirement of a consolidated return for the year 1918 and the existence of an agreement that the tax shown to be due on that return should be assessed entirely against the parent company, the status of the Louisville Woolen Mills in respect of the tax so assessed continued to be that of a taxpayer, decided an important Federal question in a way probably

in conflict with the decisions of other circuits and with the applicable decisions of this Court.

(3) The Circuit Court of Appeals, in deciding that petitioner, as surety on the bond, was not entitled to the benefit of the $30,000 paid by the Louisville Woolen Mills to the parent company as a contribution toward the consolidated liability, after the giving of the bond and after the Commissioner had ruled that a consolidated return alone was proper, and that the entire tax shown to be due thereon was assessable against the parent company, and in reliance upon such ruling, decided an important question of Federal law, and in a way probably in conflict with the decisions of other circuits, of the Court of Claims and of the United States Board of Tax Appeals.

V.

PRAYER FOR WRIT.

WHEREFORE, your petitioner respectfully prays that a writ of certiorari issue out of and under the seal of this Honorable Court, directed to the United States Circuit Court of Appeals for the Sixth Circuit, commanding said Court to certify and send to this Court for its review and determination a full and complete transcript of the record and all proceedings of the said Court had in this case, numbered and entitled on its docket Number 8596, Royal Indemnity Company, Appellant, v. United States of America, Appellee, to the end that this cause may be reviewed and determined

by this Court, and that the decree of said Circuit Court of Appeals may be reversed, and for such further relief as to this Court may seem proper.

ROYAL INDEMNITY COMPANY,
Petitioner,

By CHAS. I. DAWSON AND
ARTHUR W. GRAFTON,
Counsel for Petitioner.

WOODWARD, DAWSON & HOBSON,
GRAFTON & GRAFTON,
Of Counsel.

Supreme Court of the United States

OCTOBER TERM, 1941.

ROYAL INDEMNITY COMPANY, - - *Petitioner,*

v.

UNITED STATES OF AMERICA, - - *Respondent.*

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

I.

OPINION OF THE COURT BELOW.

The opinion of the United States Circuit Court of Appeals for the Sixth Circuit is reported in 120 Fed. (2d) beginning at page 136. A copy of the opinion is likewise annexed to this petition as Appendix A.

The memorandum opinion of the United States District Court for the Western District of Kentucky was filed September 20, 1939, and appears on page 61 of the Record, and is unreported. The District Court's opinion did not discuss the merits of the questions, but dealt purely with procedure.

II.

JURISDICTION.

Section 347 of Title 28 U. S. C. A. (Section 240 of the Judicial Code) is relied upon to sustain the jurisdiction of this Court to review the judgment of the Circuit Court of Appeals for the Sixth Circuit. The opinion in that Court was delivered on June 4, 1941, and a petition for rehearing was denied on the 9th day of October, 1941. This petition is filed within three months from that date as provided by Section 350, Title 28 U. S. C. A. (Section 240(c) of the Judicial Code).

III.

STATEMENT OF THE CASE.

The statement in the preceding petition for a writ of certiorari, Paragraph I, is hereby adopted and made a part of this brief without further elaboration.

IV.

SPECIFICATIONS OF ERROR.

Petitioner intends to urge and rely upon each of the following errors:

1. The Court erred in holding that the Commissioner could make a ruling on the bond that the subsidiary owed the tax individually after the Board of Tax Appeals and the Circuit Court of Appeals had

judicially and finally determined that the taxes for the year 1918 were assessable against and collectible from the parent corporation alone.

2. The Court erred in holding that the subsidiary's status as a taxpayer was not altered by the filing of the consolidated return, and the final judicial determination that there existed in connection with that return an agreement between the corporations that all of the tax shown to be due by such consolidated return should be assessed against and paid by the parent corporation.

3. The Court erred in holding that the surety upon the bond should not have the benefit of the $30,000.00 payment made by Louisville Woolen Mills as a contribution toward the consolidated tax liability of the parent, after the execution of the bond and after and in reliance upon the ruling of the Commissioner that a consolidated return alone was proper and that all of the taxes for the affiliates for the year 1918 should be assessed against and paid by the parent corporation.

V.

ARGUMENT.

POINT I. In August, 1932, the Commissioner Was Without Power to Rule that the Subsidiary Owed Any Part of Its Individual 1918 Taxes Inasmuch as Prior to that Time It Had Been Judicially Determined by the United States Board of Tax Appeals and the Sixth Circuit Court of Appeals that (1) the Corporations Were Affiliated, (2) a Consolidated Return Was Required (3) an Agreement Existed Between the Affiliated Corporations that All of the Taxes Found to Be Due on the Consolidated Return Should Be Assessed Against and Collected From the Parent Alone.

As the statement of the case will show, the bond here in suit was given by Louisville Woolen Mills, as principal, and petitioner as surety in connection with Louisville's claim for abatement of a part of the tax assessed against it on its 1918 individual return. At the time the bond was given no other return was contemplated. The bond guaranteed payment only of the taxes found to be due by the Commissioner from Louisville on account of that individual return. It was designed to protect the Commissioner and Collector in the event that the Commissioner in the exercise of his administrative discretion should determine that Louisville's claim for abatement was without merit in whole or in part. As was pointed out in the opinion of the Court below, it was then collectible whether erroneously returned and assessed or not. Adminis-

trative discretion in the collection of the taxes was then vested in the Commissioner.

Long after the giving of the bond, however, the Commissioner himself recognized the error of the individual returns and required in lieu thereof a consolidated return for all of the affiliated corporations. This return was filed in accordance with the Commissioner's ruling. The Commissioner's ruling was clearly correct.

During the entire year 1918, Section 240 of the Revenue Act of 1918 (40 Stat. 1057, 1081) was in full force and effect, that section providing as follows:

> "(a) That corporations which are affiliated, within the meaning of this section, shall under regulations to be prescribed by the Commissioner, with the approval of the Secretary, make a consolidated return of net income and invested capital, and the taxes thereunder shall be computed and determined upon the basis of such return. * * *
>
> "In any case in which a tax is assessed upon the basis of a consolidated return, the total tax shall be computed in the first instance as a unit and shall then be assessed upon the respective affiliated corporations, in such proportions as may be agreed upon among them, or in the absence of any such agreement, on the basis of the net income properly assignable to each.
>
> "(b) For the purpose of this section, two or more domestic corporations shall be deemed to be affiliated (1) if one corporation owns directly, or controls * * * substantially all of the stock of the other or others * * *."

The correctness of the Commissioner's ruling was never challenged by either the parent corporation or any of the affiliates and was admitted in the subsequent proceedings before the Board of Tax Appeals.

The Commissioner then went further and insisted that there existed between the affiliated corporations an agreement that all of the taxes of the affiliates for the year 1918 having been computed upon the basis of the consolidated return, as required by the statute, should be allocated to, assessed against, and collected from the parent corporation alone. The statute above quoted clearly contemplated that such agreements, if made, should be effective. The Board of Tax Appeals and the Courts have uniformly held that such an agreement, if made, is mandatory both upon the Commissioner and the corporation. *Hutchinson Coal Co.* v. *Commissioner,* 24 B. T. A. 973; *Shaeffer Pen Co.* v. *Commissioner,* 27 B. T. A. 1056; *Fidelity National Bank* v. *Commissioner* (8 C. C. A.), 39 Fed. (2d) 58; *Ford Motor Company* v. *United States,* 9 Fed. Supp. 590 (Court of Claims); *Trustees, etc.,* v. *Commissioner of Internal Revenue* (4 C. C. A.), 43 Fed. (2d) 782.

The parent corporation vigorously resisted the Commissioner's contention as to the existence of such an agreement, taking an appeal to the Board of Tax Appeals, at the hearing of which it abandoned all contentions for the year 1918 except its contentions that the Commissioner had erred in finding that such an agreement existed.

The Board of Tax Appeals by its lengthy and well-considered opinion (23 B. T. A. 670, 690, 691, 696, 697,

698) discloses the issue before it and its decision thereon with such clarity and force that we quote therefrom:

> "Petitioner denies the existence among the members of its affiliated group of any agreement for the allocation of the taxes for the years 1917, 1918 and 1919. The respondent contends that there was either an expressed or implied agreement that the entire consolidated profits tax of the group for the year 1917, and the consolidated income and profits taxes for the years 1918 and 1919, should be allocated to petitioner (690).
>
> "* * *
>
> "* * * In the instant case we believe that the facts demonstrate the existence of such an agreement and that the tax should be allocated in accordance with it, even though it does not appear that the agreement was in writing or that the respondent was given express notice of it. * * * (691).
>
> "* * *
>
> "* * * We are of opinion that the entire history of the consolidated returns of the affiliated group for the years 1917, 1918 and 1919 indicates an agreement among the affiliates, either active or passive, that the consolidated income and profits taxes of the group be allocated to petitioner, and this means that our determination involves the Louisville Company as well as the three subsidiaries just discussed (696).
>
> "* * *
>
> "Discussion of each factor influencing our determination is impracticable because the factors are too numerous. Our decision is not based upon the theory of estoppel advanced by the respond-

> ent and to the extent that it may result in the payment of consolidated taxes upon income on which taxes have already been paid by the companies severally, is reluctantly rendered. We are, however, of opinion that there existed among the petitioner and its subsidiaries an agreement that consolidated tax liabilities of the affiliated group for the years 1917, 1918, and 1919 should be allocated for assessment to petitioner alone. * * *" (697-698).

This opinion was promulgated June 12, 1931, after review by the entire Board and judgment under Rule 50 was entered January 16, 1932.

The Board was affirmed by the Circuit Court of Appeals for the Sixth Circuit on February 16, 1934 (68 Fed. (2d) 820), the language of the Circuit Court's opinion appearing on page 823 being equally clear and conclusive as follows:

> "We think there can be little doubt upon the facts stated that petitioner (American Textile Woolen Company) intended that the taxes for the years in question should not only be assessed against, it but that they should be paid by it; * * *. We think there is substantial evidence in the course followed by these officers in representing all of the companies throughout the whole controversy, to show an agreement among them all that the entire tax against the group should be assessed against and paid by the parent company. See *In re: Temtor Corn and Fruit Products Co.* (D. C.), 299 Fed. 326, 329. It is difficult to think otherwise. We think without a reiteration of the

facts that the Commissioner was justified in making the assessment from this inference."

(Certiorari was denied by this Court October 8, 1934, 293 U. S. 558.)

Thus prior to the exercise of the administrative discretion granted to the Commissioner by statute and contemplated by the terms of the bond, there had been a ruling by the Commissioner that the return mentioned in the bond was erroneously filed; that the taxes assessed on the basis of that return and mentioned in the bond were erroneously assessed; that a consolidated return should be filed in lieu thereof; that the taxes computed on the basis of the consolidated return should be assessed solely against the parent corporation; and the Commissioner's position in all of these respects over the vigorous opposition of the parent corporation had been decided in his favor by the Board of Tax Appeals.

The Commissioner did not seek to review the action of the Board of Tax Appeals, but resisted the appeal of the parent corporation from the Board to the Sixth Circuit Court of Appeals. Prior to the institution of suit upon the bond (the complaint was filed August 12, 1936 (R. 1)) the action of the Board of Tax Appeals had become final by reason of the affirmance by the Sixth Circuit Court of Appeals and the denial of certiorari by this Court.

We respectfully submit that the decisions above quoted were *res adjudicata* of all issues concerning which the administrative discretion of the Commis-

sioner was to be exercised, and that his attempted action in making a contrary ruling in August, 1932, should be adjudged a nullity.

This case is easily distinguished from cases in which an erroneous ruling may have been made by the Commissioner during the period in which administrative discretion rested in the Commissioner. Thus, in the leading case from this Court, *United States* v. *John Barth Company,* 279 U. S. 370, defense was made to an action upon a similar bond upon the ground that at the time payment of the bond was sought to be enforced, limitations had run against the collection of the tax, and this Court very properly held that the object of the giving of the bond was to obtain delay in the collection of the tax and the delay could not therefore be pleaded as a proper defense. The *John Barth case* went no further than this proposition, although its language has been used to extend its implications far beyond this doctrine. In the *Barth case* there had not been any determination binding upon the Commissioner as to the existence of the liability for the taxes guaranteed by the bond, nor in fact was there any contention made on the merits of the taxes except on the question of limitation. *Simmons Manufacturing Company* v. *Routzahn,* 62 Fed. (2d) 947 (6 C. C. A.), likewise dealt with a question of limitation and held that the giving of the bond even after the expiration of limitations constituted a waiver of limitations.

Certainly none of these cases have gone so far as to hold that the Commissioner could take one position, fight it through the Board of Tax Appeals and the Cir-

cuit Court of Appeals, have that position finally sustained, and then make a contrary ruling maturing liability on a bond such as this.

The Commissioner's actual participation in the prior litigation and its final determination in his favor certainly distinguishes the present case from cases such as *Bowers* v. *American Surety Company* (2 C. C. A.), 30 Fed. (2d) 244, where the prior adjudication of non-existence of tax liability was in an action to which the United States was not, and refused to become, a party.

To permit the Commissioner of Internal Revenue to take such a course of action is to sanction conduct on behalf of the Government which in a private individual would be characterized as fraudulent and lacking in good faith.

The question thus presented is an important one of federal law which has not been, but should be, decided by this Court.

POINT 2. The Court Erred in Holding that Louisville's Status as a Taxpayer Was Not Altered by the Filing of the Consolidated Return and the Final Judicial Determination that There Existed in Connection with That Return an Agreement Between the Corporations that All of the Tax Shown to Be Due by Such Consolidated Return Should Be Assessed Against and Paid by the Parent Corporation.

The decision of the case by the Court below included, and in fact depended upon, the conclusion expressed (120 Fed. (2d) 138) that the filing of the consolidated return in lieu of the individual returns and the assessment of the entire tax liability of the group of affiliates against the parent company did not alter the status of Louisville as a taxpayer.

This conclusion is, we submit, in conflict with the opinions of other Circuit Courts of Appeal and with the decisions of the Court of Claims.

The Internal Revenue Code (*Section 3797*), and, so far as we have been able to ascertain, all of the prior Revenue Acts have defined a taxpayer as "any person, trust estate, partnership, company or corporation subject to a tax imposed by the act," and this definition of the term has been repeatedly adopted by the courts. Thus the Fifth Circuit Court of Appeals in the case of *White* v. *Hopkins,* 51 Fed. (2d) 159, discusses at some length the meaning of the term "taxpayer," and comes to the sound conclusion that a "taxpayer is a person or corporation subject to, exposed to, or made liable for a tax." The Court of Claims in the

case of *Ford Motor Company* v. *United States,* 9 Fed. Supp. 590 (January 14, 1935), a case directly involving the sections of the 1918 statute here involved, said as follows:

> "When the members of the affiliated group agree among themselves as to the apportionment of the tax, the assessment of the tax in accordance with the agreement is mandatory under the statute, and, when the assessment of the entire tax, as in this case, is made against a single member of a group, the corporation against which the assessment is made becomes the taxpayer within the meaning of the statute and is alone entitled to refund or credit of any over-payment of the tax. This is so well settled that citation of authorities in support of the proposition is unnecessary."

This Court denied certiorari *November 11, 1935* (296 U. S. 636, 80 L. Ed. 452).

The Court of Claims in the case of *Myersdale Fuel Company* v. *United States,* 44 Fed. (2d) 437 (November 3, 1930), held that a parent corporation was a taxpayer in respect of taxes paid by it to the Government on a consolidated return only to the extent that such payment was from its own funds and represented its own liability. In that case a consolidated return was filed, and all of the tax was actually paid to the Collector by the parent, but as between the corporations the entire tax was apportioned in relation to their net incomes, and the subsidiaries furnished the parent their respective shares of the consolidated tax. The

opinion clearly holds that inasmuch as each of the affiliated corporations was liable for its portion of the consolidated tax, the affiliated corporations were therefore each taxpayers.

The Fifth Circuit Court of Appeals in the case of *Houston Street Corporation* v. *Commissioner of Internal Revenue,* 84 Fed. (2d) 821 (July 15, 1936), had before it the single question of whether the plaintiff was a taxpayer within the definition of that term contained in the Revenue Acts. The Board of Tax Appeals had concluded that it was without jurisdiction to review the action of the Commissioner because the complaining party was not a taxpayer, although the Commissioner was seeking to collect a tax from the appellant. The Court pointed out that the appellant was a taxpayer because it was liable for the tax and was therefore a person subject to the tax.

This Court, in the case of *United States* v. *Updike,* 281 U. S. 489 (May 19, 1930), decided that limitations applicable to actions against taxpayers were also a bar to an action against transferees of the taxpayers, holding that the transferee being made liable for the payment of the tax became in fact the taxpayer.

Indeed, a careful search of the authorities indicates conclusively that whether or not a corporation is a taxpayer depends upon whether or not the law imposes upon that corporation the liability for a tax or subjects that corporation to a tax.

If a corporation is not liable for a tax, it is not a taxpayer, even though it actually makes payment of

the tax on behalf of some other person or corporation actually liable therefor by law.

Thus in the instant case, at most Louisville's status as a taxpayer remained only so long as it was liable for taxes for the year in question, and when it was judicially determined that the liability for all of the taxes for the year 1918 fell upon the parent corporation by reason of the affiliation and by reason of the existence of an agreement so allocating the taxes computed upon the consolidated return, Louisville's status as a taxpayer disappeared.

The cases cited by the opinion of the Court below in support of the erroneous conclusion thus announced do not support that conclusion. The cases of *Swift & Company* v. *United States* (Court of Claims), 38 Fed. (2d) 365, and *Sweets & Company* v. *Commissioner* (2 C. C. A.), 40 Fed. (2d) 436, held only that members of an affiliated group were taxpayers because of the absence of an agreement allocating the tax to some one or more of the other members of the affiliated group, and those opinions emphasize again the test by which a corporation's status as a taxpayer is determined. Those affiliated corporations were held to be and remained taxpayers because, and solely because, of the fact that in the absence of an agreement they remained liable for their proportionate part of the consolidated tax.

The case of *Commissioner* v. *Ben Ginsburg Co.* (2 C. C. A.), 54 Fed. (2d) 238, dealt with the affiliation of two corporations where one earned income and the other sustained a loss. There was no agreement ap-

portioning the consolidated tax, and it was held that the corporation sustaining a loss in the year in question was not a taxpayer because there was properly assignable to it no part of the consolidated tax.

Clearly, then, the Second Circuit by the very case cited, namely, that of *United States* v. *Ben Ginsburg Co., supra,* decided that a corporate member of an affiliated group was not a taxpayer where it was not by law liable for a part of the consolidated tax, a conclusion directly in conflict with the decision of the Court below in the present case.

We must again point out that this result was not thrust upon the Commissioner, but was actively sought by him when he contended that an agreement existed under which all of the taxes computed on the consolidated return were to be allocated to the parent corporation. He himself successfully sought to eliminate all of the subsidiaries, including Louisville, as taxpayers, and prior to the institution of this action his position had been finally and conclusively determined by the Board of Tax Appeals and the Circuit Court of Appeals for the Sixth Circuit.

POINT 3. The Court Erred in Holding that the Surety Upon the Bond Should Not Have the Benefit of the $30,000.00 Payment Made by Louisville as a Contribution Toward the Consolidated Tax Liability of the Parent, After the Execution of the Bond and After and in Reliance Upon the Ruling of the Commissioner that a Consolidated Return Alone Was Proper, and that All of the Taxes for the Affiliates for the Year 1918 Should Be Assessed Against and Paid by the Parent Corporation.

We state again the sequence of events to emphasize this point. The subsidiary first filed an individual return for the year 1918 and paid three quarterly installments of the tax assessed on that return, leaving a balance of $32,341.24 due on December 15, 1919. It asked for abatement of this installment on the grounds that special assessment under Sections 327 and 328 of the Revenue Act of 1918 would reduce its liability. The bond was given to protect the Government during consideration of this claim in abatement.

Almost a year later the Commissioner ruled that the whole return was erroneously filed and that the parent should have filed a consolidated return. In compliance with this ruling, the parent filed the return, including in the consolidated return all of the income of the affiliates. The Commissioner then ruled that all of the resulting taxes should be assessed against the parent and no part of it allocated to the subsidiaries. The Commissioner ruled that a large additional sum was thereby due from the parent.

Relying upon this ruling, and solely because of it, the subsidiary sent to the parent $30,000.00 which the parent in turn paid over to the Collector as a payment on account of the taxes which the Commissioner was then asserting against the parent alone. The parent resisted the proposed allocation of all of the tax to the parent, and thirteen years after the bond was given and twelve years after the subsidiary had contributed the $30,000.00, the Commissioner's position was sustained by the Board of Tax Appeals. Then for the first time since the giving of the bond, and at a time when the subsidiary had become insolvent, the Commissioner demanded of the subsidiary the payment of the balance of its original 1918 taxes. Both the District Court and the Circuit Court of Appeals have failed to give to the surety any credit for the payment made by its principal. The Court below disposed of the surety's contention in this connection by a statement having no foundation in fact. This statement is as follows:

> "Moreover, Louisville's share in the aggregate tax liability amounted to $167,520.57. Its three installments of taxes paid, its fourth installment secured by the bond, and its $30,000.00 contribution to the $100,000.00 paid on account by American, do not, in the aggregate, liquidate the sum assignable to it as its share of the total tax liability of the affiliated companies."

As we have heretofore pointed out in Point 2, it was determined by the Board of Tax Appeals and by the Sixth Circuit Court of Appeals in the prior litiga-

tion, that Louisville had no share of the aggregate tax liability revealed by the consolidated return. In fact, as we have pointed out, the prior litigation involved only the issue as to whether the subsidiaries should have assessed against them their proportionate part of the aggregate consolidated tax.

Furthermore, the figure of $167,520.57 appears in the Record for the first time in the opinion of the Court below. Neither the Government in its original complaint, which was the only pleading ever filed by the United States, nor the petitioner in its original and its amended answer ever alleged the existence of liability on Louisville in such an amount.

This figure was in fact suggested to the Court below in the Government's brief in that Court, in which it was pointed out that the Board of Tax Appeals had found (23 B. T. A. 682) that if the consolidated tax were apportioned to the affiliated corporations as though no agreement for allocation existed, Louisville's share of such consolidated tax would have been $167,520.57.

The only way in which the conclusion could properly be reached that Louisville's share of the aggregate tax liability was the sum named, was to find that no agreement existed between the corporations allocating the consolidated tax for assessment and collection against the parent corporation alone. When the Board of Tax Appeals found that the agreement did in fact exist, this figure became meaningless. It is, therefore, manifestly erroneous to now refer to the figure as having some bearing on the tax liability of Louisville, or

on the question of whether the surety should be given credit for the $30,000.00 payment made by Louisville after the execution of the bond.

The Commissioner could have agreed with American Textile Woolen Company that no agreement existed for the allocation of the consolidated tax and could have thereby fixed Louisville's share thereof at $167,520.57. He refused to do so and litigated for many years to sustain his position. He should not now be permitted to assert that Louisville's liability was ever such a sum.

Furthermore, no additional assessment against Louisville has ever been proposed by the Commissioner since Louisville filed its original individual 1918 return. By that return it showed a total individual tax liability of $129,364.93, and admittedly paid all of that except $32,341.24 (R. 2, 3). No action has been taken by the Commissioner, nor by anyone else, to assert as against Louisville any additional tax for the year 1918. Its maximum liability, therefore, was $32,341.24 on December 15, 1919, when the bond in question was given, and that liability has only been increased by statutory interest. Louisville was stricken from the record before the Board of Tax Appeals upon the ground that no additional taxes were being asserted against it. Nothing that was done in connection with the filing of the consolidated return resulted in the increase of its liability, nor has the Government ever so contended, until its counsel filed a brief before the Circuit Court of Appeals in this action.

Meanwhile, in 1921 in reliance upon the position taken by the Commissioner, Louisville paid $30,000.00 through its parent to the Collector. To deny the surety the benefit of this payment is to completely disregard the rights of the surety, as its principal has clearly performed in part the obligation guaranteed by the bond.

Performance by the principal is a complete defense to an action on such a bond. See *United States* v. *Erb,* 79 Fed. (2d) 538. Partial performance operates likewise as a release *pro tanto.*

Even assuming that it is possible to conclude that the subsequent action of the Commissioner in requiring a consolidated return would increase the liability of Louisville for taxes for the year 1918, still the $30,000.00 must be credited against the earlier liability and the surety should be given the benefit of that payment. See *Columbia Digger Company* v. *Rector,* 215 Fed. 618; *United States* v. *Brent,* 236 Fed. 771; *United States To Use of Thomas* v. *Morgan,* 111 Fed. 490.

VI.

CONCLUSION.

It is therefore respectfully submitted that this case is one calling for the exercise by this Court of its supervisory power, in order that important questions of federal law may be promptly, finally, and authoritatively determined; and to that end a writ of certiorari should be granted and this Court should review

and reverse the decision of the United States Circuit Court of Appeals for the Sixth Circuit.

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APPENDIX A.

(Filed June 4, 1941, John W. Menzies, Clerk.)

Nos. 8596-97.

UNITED STATES CIRCUIT COURT OF APPEALS
SIXTH CIRCUIT.

ROYAL INDEMNITY COMPANY,
Appellant,

v.

UNITED STATES OF AMERICA,
Appellee,

AND

UNITED STATES OF AMERICA,
Appellant,

v.

ROYAL INDEMNITY COMPANY,
Appellee.

Appeal from the District Court of the United States for the Western District of Kentucky.

Decided June 4, 1941.

Before Hicks, Simons and Martin, Circuit Judges.

Simons, Circuit Judge. The appeal challenges the liability imposed on the appellant as surety for the Louisville Woolen Mills under a bond filed with the Commissioner of Internal Revenue for the purpose of securing the United States in the collection of the final installment of income and excess profits tax for the year 1918.

For that year the Louisville Woolen Mills filed its individual tentative return showing taxes due from it in the amount of $129,364. It paid the first three quarterly installments upon its tax liability, but before the last payment of $32,341 became due the taxpayer filed its claim for abatement, asserting that it was entitled to the benefits of the special assessment provision, §§327 and 328 of the Revenue Act of 1918. It asked that collection of this installment be postponed until the claim for abatement had been passed upon, and its request was granted upon condition that it execute a bond to secure the United States in the collection of the postponed installment. The bond as executed recited that it was "in consideration of withholding collection of said taxes at this time and until such time as the Honorable Commissioner of Internal Revenue may pass upon the claim for abatement of said assessed taxes filed by the principal herein, and in order to protect the United States Government and Elwood Hamilton, Collector of Internal Revenue of the Kentucky District, against any loss, cost or damage by reason of the said claim for abatement." The bond further recited that the principal and surety bound themselves "to hold the said Elwood Hamilton, Collector of Internal Revenue as aforesaid, entirely harmless from all loss, costs, and damages he may sustain by reason of his having given to the said principal, that is, the Louisville Woolen Mills, an extension of time within which to obtain a final ruling from the Honorable Commissioner of Internal Revenue as to the liability of said Louisville Woolen Mills for the said assessment; and further to pay the sum of $32,341.24, or as much thereof, if any, as the Honorable Commissioner of Internal Revenue shall find from his rulings to be due to the United States from the said Louisville Woolen Mills on account of the said assessment, with interest thereon at the rate of one per cent per month from the 15th day of

December, 1919, together with all costs and penalties thereon which may accrue."

On October 26, 1920, without having acted upon the claim of abatement, the Commissioner, by letter, advised the American Textile Woolen Company with which the taxpayer was affiliated, that a consolidated return was required under subsection (b) of §240. See *American Textile Woolen Co.* v. *Commissioner*, 68 Fed. (2d) 820 (C. C. A. 6). The American Textile Woolen Company complied and on February 12, 1921, filed a consolidated return for itself and affiliates, including the Louisville Woolen Mills, and on October 7, 1925, the Commissioner advised it of a final determination of deficiencies that he proposed to assess in their entirety against American. An appeal to the Board of Tax Appeals followed, resulting in a decision by the Board that the tax due upon the consolidated return should be assessed in its entirety against America, and that there was a deficiency of $39,362 in the payment of its tax. This was arrived at by crediting upon the aggregate tax liability of the affiliated corporations the taxes assessed against each upon their separate returns and crediting a payment of $100,000 paid by American to apply on the total liability. Of this amount Louisville contributed $30,000. In crediting against the aggregate tax liability of the group the amounts assessed upon the original separate returns of the affiliated corporations, the Commissioner allowed a credit to American not only the three installments of 1918 taxes paid by Louisville, but also the fourth installment, which, though unpaid, had been secured by its bond with the appellant as surety.

On August 23, 1932, the Commissioner advised Louisville that he had rejected its claim for abatement. He made demand upon it for the payment of the postponed installment, and upon the failure to obtain payment instituted the present suit against the surety of its bond.

While Louisville as principal was made a party defendant, it was so hopelessly insolvent that it was never brought into court and no judgment was rendered against it. A demurrer to the complaint was overruled and judgment entered for the United States in the court below for the face of the bond with interest at the rate of six per cent per annum from December 15, 1919, until paid. The surety appeals from the judgment, asserting non-liability, and the United States cross-appeals because of an asserted inadequate allowance of interest.

The appellant contends that there was no ruling on the part of the Commissioner maturing its liability upon the bond. It points to the language of that instrument as limiting its liability to pay the sum of $32,341.24 on account of an assessment originally made against its principal. It urges that upon the filing of the consolidated return and the assessment of the tax in its entirety against American, the individual assessment against Louisville was, in effect, expunged and nullified, and since no new assessment was ever made against Louisville for any portion of the tax, the obligation of the surety, under the terms of the bond, never attached. On the other hand, the government insists that the appellant is attacking the Commissioner's determination of a tax liability asserted against its principal, and that this may not be done collaterally under the adjudicated cases.

At the time the bond was executed there was an assessment against the principal upon its individual tax return. The Commissioner could have enforced collection of the unpaid fourth installment thereof. It was an act of grace to permit the taxpayer to postpone payment until the claim for abatement should be acted upon, and to permit it to substitute the bond for the obligated payment. That thereafter a consolidated return was filed leading to an assessment of the entire tax liability of the group of

affiliates against American did not alter the status of Louisville as a taxpayer, nor did it release the surety from its obligation upon its bond. An affiliated group filing a consolidated return becomes a tax computing unit. It is not a taxable unit. *Commissioner of Internal Revenue* v. *Ben Ginsburg Co.*, 54 Fed. (2d) 238 (C. C. A. 2); *Sweets Co.* v. *Commr.*, 40 Fed. (2d) 436 (C. C. A. 2); *Swift & Co.* v. *U. S.*, 38 Fed. (2d) 365, 379 (Ct. Cl.). The application of payments made on the individual assessments of the affiliates to the tax liability of the group was assumed, upon a substantial factual basis, to have been made with their consent. *American Textile Woolen Co.* v. *Commr., supra,* 823. It must also be assumed that the credit for the fourth installment secured by the bond was likewise with the consent of Louisville. Moreover, Louisville's share in the aggregate tax liability amounted to $167,520.57. Its three installments of taxes paid, its fourth installment secured by the bond, and its $30,000.00 contribution to the $100,000.00 paid on account by American, do not, in the aggregate, liquidate the sum assignable to it as its share of the total tax liability of the affiliated companies.

It must not be forgotten that the suit is on the bond and not for the collection of a tax. The liability for the tax as tax may have been terminated, though this we do not decide, or, as in *U. S.* v. *John Barth Co.*, 279 U. S. 370, collection may become impossible because of the running of time, but this has no bearing upon the obligation of the surety upon the bond. As was said in the Barth case, "the object of the bond was not only to prevent the immediate collection of the tax, but also to prevent the running of time against the government. The taxpayer has obtained his object by the use of the bond and he should not object to making good the contract by which he obtained the delay he sought." As pointed out in *Simmons*

Mfg. Co. v. *Routzahn*, 62 Fed. (2d) 947 (C. C. A. 6), "but for the bond the collector could have made collection."

In insisting that the appellant's liability was not matured because limited to taxes due the United States "on account of said assessments," the appellant overlooks the fact that the surety undertook to hold the collector harmless from all loss and damages he might sustain by reason of his having given to the principal an extension within which to obtain a final ruling, and the further obligation of the surety to pay the sum of $32,341.24, or as much thereof, if any, as the Commissioner shall find from his rulings to be due the United States. The Commissioner, by his demand for collection, made the ruling contemplated by the bond, and it is not within the province of the surety to insist collaterally upon formalities perhaps imperative in the collection of a tax. The obligation is one of contract.

Since the obligation of the bond was to save the collector harmless from any loss he might sustain by reason of his having granted the extension, interest was properly limited to the amount collectible from the taxpayer under the statute, which, by §250(e), limits recovery to one-half per cent per month to the date of the rejection of the claim, and to twelve per cent per annum thereafter until paid. This result has the approval of the authorities. *U. S.* v. *Erb*, 79 Fed. (2d) 538 (C. C. A. 2); *Maryland Cas. Co.* v. *U. S.*, 76 Fed. (2d) 626 (C. C. A. 5).

The judgment below in favor of the United States is affirmed. The cross-appeal of the government is dismissed.

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CITATIONS

Cases:

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433532—41



In the Supreme Court of the United States

OCTOBER TERM, 1941

No. 781

ROYAL INDEMNITY COMPANY, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The memorandum opinions of the United States District Court for the Western District of Kentucky (R. 51–52, 61–63) are unreported. The opinion of the United States Circuit Court of Appeals for the Sixth Circuit (R. 82–86) is reported in 120 F. (2d) 136.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered June 4, 1941 (R. 81). A petition for rehearing was filed August 4, 1941 (R. 89) and

denied October 9, 1941 (R. 119). A petition for writ of certiorari was filed December 4, 1941. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

1. Whether a surety on a bond given to stay collection and secure payment of a tax pending disposition of a claim in abatement filed by the principal, against whom the tax was assessed, may avoid liability on the ground that the assessment was invalid and that therefore the Commissioner was without power to reject the claim.

2. If not, whether in any event the surety was discharged to the extent of an amount which the principal voluntarily contributed to its parent company and which was paid to the United States by the latter in part satisfaction of the latter's consolidated tax liability.

STATUTES INVOLVED

The pertinent portions of the Revenue Act of 1918, c. 18, 40 Stat. 1057 are set forth in the Appendix, *infra*, p. 10.

STATEMENT

This suit was brought by the United States against Louisville Woolen Mills, as principal, and Royal Indemnity Company, petitioner herein, as surety, to recover upon a common law bond given

to stay the collection and secure the payment of certain income and excess profits taxes pending determination of a claim in abatement filed by the principal. Summons was returned unexecuted as to the principal and there was no appearance by it (R. 9). Recovery against petitioner in the amount of $32,341.24 with interest was allowed by the district court (R. 65). Its judgment was affirmed by the court below (R. 86). The essential facts, as alleged in the complaint and admitted by the answer, are as follows:

In its tax returns for 1918, Louisville Woolen Mills, a Kentucky corporation, reported a tax liability of $129,364.93, which amount was duly assessed by the Commissioner of Internal Revenue (R. 2, 12). After payment of $96,843.71 of the tax so assessed, the taxpayer, on December 15, 1919, filed a claim for abatement of the unpaid balance of $32,341.24 on the ground that it should receive the benefit of a lower assessment authorized by Section 327 (d) and Section 328 of the Revenue Act of 1918 (R. 2–3, 12). The bond in suit was executed on the same date (R. 3, 12). It provided that:

> * * * in consideration of withholding collection of the said taxes * * * until such time as the Honorable Commissioner of Internal Revenue may pass upon the claim for abatement of the said assessed taxes * * * , and in order to protect the United States Government and Elwood

> Hamilton, Collector of Internal Revenue * * *, against any loss, cost or damage by reason of the said claim for abatement, the Louisville Woolen Mills, of Louisville, Kentucky, principal and the Royal Indemnity Company, of New York, surety, hereby bind themselves, jointly and severally * * * to pay to the said Elwood Hamilton, * * * the sum of $32,341.24, or as much thereof, if any, as the said Louisville Woolen Mills may be required * * * to pay on account of said assessment, together with interest thereon at the rate of one percent per month * * *; and, further, to pay the sum of $32,341.24, or as much thereof, if any, as the Honorable Commissioner of Internal Revenue shall find from his rulings to be due to the United States of America from the said Louisville Woolen Mills on account of the said assessment, with interest thereon * * *.

On August 23, 1932, while the bond was still in effect and the tax secured by it remained unpaid, the Commissioner wrote a letter to the taxpayer stating the following (R. 5–6, 16):

> Your claim is for abatement of part of the tax reported on your separate 1918 return and is a claim for special assessment under sections 327 and 328 of the Revenue Act of 1918. During the year 1918 your company was a subsidiary of American Textile Woolen Company, and computa-

> tion of the profits tax of the consolidation under sections 327 and 328 of the Revenue Act of 1918 was allowed by the Bureau. The Bureau's computation of the consolidated tax was appealed to the United States Board of Tax Appeals by your parent company on an issue relative to the allocation of the tax, and the Board's order entered January 16, 1932, in effect allocates to your company the amount of tax previously assessed on your return. Your claim for the abatement of part of such assessment will therefore be rejected.

Thereupon the Commissioner rejected the claim for abatement (R. 6, 16). The present suit was instituted after the taxpayer and petitioner had failed and refused to comply with the Collector's demands for payment of the $32,341.24 due with interest (R. 6, 17).

ARGUMENT

1. The principal contention (Pet. 10, 16–24) made by petitioner is that the decision in *American Textile Woolen Co.* v. *Commissioner,* 23 B. T. A. 670 (1931), affirmed, 68 F. (2d) 820 (C. C. A. 6), certiorari denied, 293 U. S. 558, precluded the Commissioner from rejecting the claim for abatement. It was there determined that under the consolidated return provisions of Section 240 of the Revenue Act of 1918 (Appendix, *infra,* p. 10) the American Textile Woolen Company was properly assessed to pay the taxes upon the com-

bined income for 1918 of it and its affiliated subsidiaries, of which Louisville Woolen Mills was one, since the evidence showed an agreement among them that the taxes should be so assessed. Petitioner construes this as a holding, in effect, that the prior assessment of $129,364.93 taxes against its principal, Louisville Woolen Mills, was erroneous and hence that the unpaid balance of $32,341.46 secured by the bond was not owing. It contends (Pet. 21–22) that for such reason the Commissioner had no discretion to require payment of any part of the amount last mentioned, that his action in purporting to do so was a nullity, and that, accordingly, it is not liable on the bond.

Thus petitioner seeks to avoid its obligation by attacking collaterally the validity of the Commissioner's denial of the claim for abatement. But this it may not do. The condition of the bond was that it would pay all or so much of the unpaid balance of the tax assessed as its principal "may be required to pay" or as the Commissioner "shall find from his rulings to be due," and it is settled law that such a promise creates an independent liability which cannot be avoided on the ground that the tax secured was uncollectible or in fact not owing. It is enough that the condition of the bond occurred, whether the Commissioner's ruling was right or wrong. *United States* v. *John Barth Co.*, 279 U. S. 370; *Gulf*

States Steel Co. v. *United States,* 287 U. S. 32; *Bowers* v. *American Surety Co.,* 30 F. (2d) 244 (C. C. A. 2d), certiorari denied, 279 U. S. 865; *Miami Valley Fruit Co.* v. *United States,* 45 F. (2d) 303 (C. C. A. 5th), certiorari denied, 283 U. S. 841; *Simmons Mfg. Co.* v. *Routzahn,* 62 F. (2d) 947 (C. C. A. 6th), certiorari denied, 289 U. S. 751; *Maryland Casualty Co.* v. *United States,* 76 F. (2d) 626 (C. C. A. 5th); *United States* v. *Oswego Falls Corp.,* 113 F. (2d) 322 (C. C. A. 2d).

No unjust enrichment of the Government or other unfairness results from holding petitioner to its word. The bond fulfilled its purpose of staying collection of the tax pending determination of the claim for abatement, and, if it had not been given, the tax presumably would have been collected. Cases, *supra.* No assessment covering Louisville Woolen Mills' income for 1918 was made against the American Textile Woolen Company until nearly two years after the claim for abatement was filed (23 B. T. A. 670, 677; see Pet. 5). In thereafter finally computing the tax which was due from American, the Commissioner allowed a credit of $395,610.74 representing the total of all assessments previously made against it and its subsidiaries, including the full amount of the assessment against Louisville Woolen Mills (23 B. T. A. 670, 682–3; R. 84). The rejection of the claim for abatement, therefore, did not

have the effect of twice taxing the same income, and recovery upon the bond herein results in no unjust enrichment.

2. Petitioner contends (Pet. 11, 29–33) that in any event the court below erred in not according it the benefit of $30,000 contributed by its principal in 1921 to American Textile Woolen Company and by the latter paid to the United States. Admittedly, however, the principal contributed that amount voluntarily and not on account of the assessment against it secured by the bond (R. 27). Nor was any portion paid to the Government on that account. The entire amount was paid, on the contrary, in part satisfaction of American's consolidated tax liability, not merely for the year 1918, but for 1917 and 1919 as well (23 B. T. A. 670, 677; 68 F. (2d) 820, 823).[1] Accordingly, there is no basis for petitioner's claim that its obligation on the bond was released pro tanto.[2]

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[1] For the year 1918, the *pro rata* share of Louisville Woolen Company for the consolidated tax liability of American was $167,520.57, computed on the basis of the respective net incomes of the affiliated companies (23 B. T. A. 670, 682). As noted by the court below (R. 85), this amount was more than the total tax of $129,364.93 assessed against Louisville separately plus the $30,000 contributed by it to American.

[2] The cases cited by petitioner are inapplicable since the payments by the principals there involved, which were held to release the sureties pro tanto, were on account of the debts which were secured by the bonds. *Columbia Digger Co.* v. *Rector*, 215 Fed. 618; *United States* v. *Brent*, 236 Fed. 771; *United States to Use of Thomas* v. *Morgan*, 111 Fed. 474.

CONCLUSION

The decision below is correct. There is no conflict of authority. The petition should be denied.

Respectfully submitted.

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DECEMBER 1941.

APPENDIX

Revenue Act of 1918, c. 18, 40 Stat. 1057:

> SEC. 240. (a) That corporations which are affiliated within the meaning of this section shall, under regulations to be prescribed by the Commissioner with the approval of the Secretary, make a consolidated return of net income and invested capital for the purposes of this title and Title III, and the taxes thereunder shall be computed and determined upon the basis of such return: * * *
>
> In any case in which a tax is assessed upon the basis of a consolidated return, the total tax shall be computed in the first instance as a unit and shall then be assessed upon the respective affiliated corporations in such proportions as may be agreed upon among them, or, in the absence of any such agreement, then on the basis of the net income properly assignable to each. * * *
>
> (b) For the purpose of this section two or more domestic corporations shall be deemed to be affiliated (1) if one corporation owns directly or controls through closely affiliated interests or by a nominee or nominees substantially all the stock of the other or others, or (2) if substantially all the stock of two or more corporations is owned or controlled by the same interests.

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